No. 87-1841

Supreme Court, U.S.
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In the Supreme Court of the United States

October Term, 1987

CITY OF SANTA MONICA, California,

Petitioner,

v.

SHELL OIL COMPANY,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

CROSS PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Are leases of subsurface municipal lands for private crude oil pipelines subject to judicial review under the Commerce Clause, or are the parties free under the Market Participant Doctrine to seek mutually acceptable terms, where the municipality, as lessor, competes with other public and private entities in the relevant and diverse market?

2. Does the Commerce Clause, in the absence of implementing Congressional action, confer upon private parties the right to permanently occupy the subsurface of city streets for their exclusive proprietary use despite the city's objection?

LIST OF PARTIES

A complete list of parties appears in the Caption and at pages iii - x of the Petition for Writ of Certiorari herein. The City of Santa Monica is a political subdivision of the State of California, operating under a Freeholders Charter.

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No. _____

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CROSS PETITION FOR WRIT OF CERTIORARI

Pursuant to Supreme Court Rules 19.5 and 20.5, the City of Santa Monica respectfully requests that a Writ of Certiorari be issued to the United States Court of Appeals for the Ninth Circuit to review its Judgment entered on October 21, 1987.[1]

OPINIONS BELOW

The Opinion of the Court of Appeals for the Ninth Circuit is reported at 830 F.2d 1052 (9th Cir. 1987) and

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[1]This Cross-Petition for Writ of Certiorari is filed contemporaneously with the City's Brief in Opposition to (Shell Oil Company's) Petition for Writ of Certiorari. This Cross-Petition is conditional on the grant of Shell's Certiorari Petition.

is reprinted as Appendix A to the Petition for Writ of Certiorari; the Order denying rehearing and rejecting the suggestion for rehearing en banc is reprinted as Appendix C.

The Memorandum of Decision and the Judgment of the District Court for the Central District of California (Honorable Robert J. Kelleher, presiding) are not reported; they are reproduced as Appendices B and D to the Petition for Writ of Certiorari.[2]

JURISDICTION

The Opinion of the Court of Appeals for the Ninth Circuit was issued on October 21, 1987; Judgment was entered the same date.

A timely petition for rehearing, filed by Shell Oil Company, was denied by Order entered on January 11, 1988.

This Cross-Petition is filed pursuant to Supreme Court Rule 19.5. A Petition for Writ of Certiorari by Shell Oil Company was docketed in this Court and received by Cross-Petitioner on April 11, 1988.

The Court has jurisdiction of the Cross-Petition pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS INVOLVED

This case involves construction of the Commerce Clause and the Tenth Amendment of the United States Constitution.

1. U.S. Const., Art. I, § 8, cl. 3 states:

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[2]Appendix (App.) citations are to the Appendix to (Shell Oil Company's) Petition for Writ of Certiorari.

> The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.

2. U.S. Const., Amend. X states:

> The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.

STATEMENT OF THE CASE

A. Nature of the Controversy.

This is an action under the Commerce Clause. Shell's complaint contends that the Clause, in its dormant state, requires that Santa Monica grant Shell a perpetual lease of the subsurface of city streets for Shell's private exclusive use. It further claims a right to such lease for a nominal fee, not to exceed the City's costs and any loss resulting from the grant. In contrast, the City does not believe the Commerce Clause was intended to confer such rights, tantamount to eminent domain, on private parties. Moreover, even if the Clause could in some cases require affirmative governmental action in aid of commerce, the City is exempt from scrutiny here since it is but one of many participants in the relevant market.

Both in its sovereign and proprietary capacities, Santa Monica asserts the right to determine whether and on what terms to grant leases to private parties. The City has proposed a fee based on the fair rental value of an exclusive subsurface easement. Any amount less than that would be contrary to the City's fiduciary responsibilities.

The judgment of the Court of Appeals, while upholding the City's mechanism for setting rental fees,

nonetheless suggests requirements for local governments which are inconsistent with the Commerce Clause and principles of federalism. The notion that private firms may appropriate permanent exclusive rights in municipal property (whether the governmental interest is proprietary or sovereign) is both novel and important. No less disturbing is the prospect of a wide range of municipal contracts having to be submitted to federal courts for approval.[3]

B. Statement of Facts

The City incorporates by reference the Statement of Facts in its Brief in Opposition to the Petition for Writ of Certiorari.

C. Proceedings Below.

The City incorporates by reference the statement of Proceedings Below in its Brief in Opposition to the Petition for Writ of Certiorari.

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[3]Shell's Complaint sought: (1) a declaratory judgment regarding the permissible terms for a new franchise; and (2) a permanent injunction "requiring defendant City to grant Shell all necessary rights required to allow Shell to continue to transport crude oil by said pipeline through the City conditioned on the payment of a fee as determined by the Court. . . ." CR 1:10.

REASONS FOR GRANTING THE WRIT

I

THE DECISION OF THE COURT OF APPEALS CONFLICTS WITH THIS COURT'S MARKET PARTICIPANT CASES AND RAISES QUESTIONS UNRESOLVED BY THE COURT'S 4-4 AFFIRMANCE IN *WESTERN OIL & GAS ASS'N v. CORY*

This case is the sequel to *Western Oil & Gas Association v. Cory*, 726 F.2d 1340 (9th Cir. 1984). The Ninth Circuit's decision in that case, rejecting the market participant doctrine[4] in reviewing pipeline easements over state coastal lands, was affirmed by an equally divided Court. 471 U.S. 81 (1985) (Powell, J., not participating). The Court of Appeals found that case controlling, although "the present case is distinguishable from *Cory*." App. A-9.

The prevailing rule is that "state proprietary functions are exempt from Commerce Clause scrutiny." *Reeves, Inc. v. Stake*, 447 U.S. 429, 437 n.9 (1980). The threshold question is "whether a particular state action more closely resembles an attempt to impede trade among private parties, or an attempt . . . to govern the State's own economic conduct and to determine the parties with whom it will deal." *White*, 460 U.S. at 218 (1983) (Blackmun, J., concurring in part). Here, the District Court answered that question in favor of market participant status. It found the parties' relationship was contractual, not regulatory; Shell's lease was the subject

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[4]"[S]tate and local governments are [not] restrained by the Commerce Clause when they seek to effect commercial transactions not as 'regulators' but as 'market participants.' " *White v. Mass. Council of Construction Employers*, 460 U.S. 204, 206 (1983).

of "arms length negotiation between parties of equal bargaining power." App. B-8.

This Court has noted three exceptions to the market participant doctrine, foreign commerce, natural resources, and restrictions on resale, *South Central Timber v. Wunnicke*, 467 U.S. 82, 96 (1984), none of which are applicable here. In *Cory*, the Ninth Circuit created two more exceptions, monopoly market position, and property held in a sovereign capacity. 726 F.2d at 1343. The first is consistent with the doctrinal basis for market participant immunity; state participation in, rather than regulatory control over, the market.[5] However, the second exception found by the court, and prominent in its decision here, is wholly inconsistent with the doctrine.

Santa Monica does not enjoy monopoly power, as did the State in *Cory*. This was the finding of the District Court on undisputed evidence. CR 78:95, 129, 215; 96:5; 80:24. Accordingly, the Court of Appeals rested its holding on its "sovereign capacity" exception. App. A-9-10. The court reasoned that when the city enters the market with land it holds in a sovereign capacity, rather than with property "purchased or acquired by the city through its entry into the real estate market," App. A-11 n.5, it is not engaged in "marketplace conduct." *Id.*

The decision of the Court of Appeals fails to recognize that state proprietary functions are not incompatible with sovereign powers. A state may exercise both authorities with respect to the same property. *Reeves,*

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[5] As explained in *Reeves*, where the state has "unique access" to the commodity being traded, such as scarce natural resources, the prospect of economic Balkanization is more problematic. 447 U.S. at 444.

447 U.S. at 439 n.12 ("[w]hen a State buys or sells, it has the attributes of both a political entity and a private business"). That Santa Monica may have acquired its property interest in the subsurface of the streets in its political capacity does not foreclose it from subsequently exercising proprietary powers.[6] A city's authority over municipal property may be described as "sovereign" when examining the breadth of its power. Thus, characterization of a city's interest in its streets as "sovereign" is usually made in the context of determining the scope of municipal authority or autonomy from state control. *See generally* 10 McQuillan, *Municipal Corporations*, §§ 30.39, 30.40 (3d ed. 1981). At the same time, a city may act as a private trader when dealing with persons seeking to acquire a commercial interest in that property.[7]

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[6]California authorizes its charter cities to act in a proprietary manner in the leasing of municipal property for non-public utility pipelines. *See e.g.*, Cal. Public Utilities Code § 6203 (city may grant franchise upon "terms and conditions . . . whether governmental or contractual in character, as in the judgment of the legislative body are to the public interest"); *id.* § 6231 (franchisee shall pay "an annual franchise fee in an amount agreed to by the applicant and the municipality").

[7]Shell argues that the City has no proprietary interests itself in subsurface property, but it may nonetheless grant such interests to third parties. It is not immediately obvious how the City might do this. If it only exercises sovereign authority, as trustee of public rights and interests, the City surely cannot allow permanent and exclusive private use. Cal. Const. Art. XVI, Section 6 (prohibiting gifts of public property); *Los Angeles County v. Southern California Tel. Co.*, 32 Cal.2d 378, 196 P.2d 773, 780 (1948) (street franchise to public utility violates state constitutional prohibition if it fails to confer sufficient public benefit). Thus, Shell's argument proves too much, because it would require Shell to obtain subsurface rights from each of the individual land owners along the route. *See Gurnsey v. Northern California Power Co.*, 160 Cal. 699, 117 P. 906 (1911).

It is the relationship between the state and commerce which determines whether the Commerce Clause applies, not whether the state acts in a "sovereign capacity" in other respects. *New England Power Co. v. New Hampshire*, 455 U.S. 331, 338-39 n.6 (1982) (market participant exemption depends on whether state is regulating use, not on manner of ownership of its property). Thus, the "single inquiry" in this case is whether the particular conduct under challenge constitutes "state participation in the market." *Reeves*, 447 U.S. at 436 n.7; *White*, 460 U.S. at 208. That sovereign interests may be simultaneously at work, does not defeat the market participant doctrine.

Accordingly, sovereign ownership of land does not preclude government from exercising proprietary control. *Western Oil & Gas Ass'n v. California State Lands Comm'n,* 105 Cal. App. 3d 554, 566, 164 Cal. Rptr. 468, 475 (1980) ("[w]hen the state leases trust lands, it is exercising a proprietary function");[8] *Los Angeles Athletic Club v. Board of Harbor Comm'nrs*, 130 Cal. App. 376, 386, 20 P.2d 130, 134 (1933) (lease of public trust lands is a proprietary, not governmental, function). Indeed, the Court of Appeals' rejection of Santa Monica's proprietary interest in municipal property is inconsistent with its contemporaneous holding that lease rent constitutes a "user fee." *See Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 622 n.12 (1981) (" 'user' fees 'partake of the nature of a rent charged by the State, based upon its proprietary interest in its public property' ") (citing P. Hartman, *State Taxation of Interstate Commerce*, 122 (1953)).

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[8]The cited case resolved the state issues in *Cory*, upon abstention by the District Court.

The inadequacy of the Court of Appeals' revision to the market participant doctrine is well illustrated by the instant case. Santa Monica exercises control over Shell's subsurface pipeline only to the extent specified in a freely negotiated lease; no more than any private landowner. For the City to benefit from the lease, it must not bargain so hard as to motivate Shell, its only customer[9], to utilize alternatives available to it. The City is thus constrained by the free market in dealing with Shell. Santa Monica's interest, like that of any private trader, is to get fair value for use of its property, not to impede trade or secure advantage for domestic commerce.

The "sovereign capacity" exception created by the Court of Appeals is inconsistent with this Court's market participant cases.[10] Because it raises an important and recurring issue, review is warranted.

II

THE DECISION OF THE COURT OF APPEALS, SUGGESTING THAT SANTA MONICA MUST YIELD SOVEREIGN PROPERTY WHERE NECESSARY TO FACILITATE INTERSTATE COMMERCE, RAISES IMPORTANT ISSUES OF FEDERALISM

Shell claims that Santa Monica has no option but to lease city streets to firms engaged in commerce.

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[9]Rather than Santa Monica being a monopolist, Shell is a monopsonist, since it is the only private user of subsurface municipal land. App. A-12, B-6.

[10]Indeed, sovereign ownership would seem to support, not undermine, use of the market participant doctrine. *Reeves*, 447 U.S. at 438 ("[r]estraint in this area is also counseled by considerations of state sovereignty, the role of each State 'as guardian and trustee for its people' ").

Indeed, by its own characterization of the issue, Shell uses the dormant Commerce Clause to compel the City to "surrender" property rights.[11] The Court of Appeals implicitly accepted the claim by suggesting that a decision not to award a franchise would be subject to Commerce Clause scrutiny.[12] If the court is correct in its conclusion that "this case involves lands held in a sovereign capacity," App. A-10, forcing the City to yield proprietary interests in such lands raises serious federalism concerns.

States, in the exercise of sovereign prerogatives, might ordinarily find their basic protection in the "structure of the federal system" rather than in judicial enforcement of Tenth Amendment constraints. *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528, 551 (1985). More recently, this Court emphasized in *South Carolina v. Baker*, ___ U.S. ___, 56 U.S.L.W. 4311 (April 20, 1988), that the political process itself is the principal guarantor of structural federalism. But the instant case involves no affirmative expression of federal policy or congressional oversight.[13] Because Shell's demand for proprietary rights in sovereign state property is made to the judiciary, not Congress, the structural safeguards that were critical in *Garcia* and *Baker* are absent here.

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[11]See Cert. Pet. at 6; CR 1:10; "Issues Presented For Review," Appellant's Opening Brief in the Court of Appeals at 1.

[12]The court stated "in deciding *whether*, or on what terms, to grant a franchise for the use of public streets the city may not burden interstate commerce in a manner that violates the dormant Commerce Clause." App. A-11 (emphasis added).

[13]Indeed, Congress has rejected exercising any authority regarding the routing of crude oil pipelines. See 49 U.S.C. § 2001(4) (Hazardous Liquid Pipeline Safety Act) ("this chapter does not authorize the Secretary [of Transportation] to prescribe the location or the routing of any pipeline facility").

The core question is whether the Commerce Clause, by its own force, has divested the States of power to control the disposition of sovereign property. It does to some extent where that property has been dedicated to traditional public transportation uses; a classic focus of the nation-unifying theme of the Commerce Clause. *Cooley v. Board of Wardens*, 55 U.S. (12 How.) 299 (1851).[14] The rule is inappropriate, however, where State property has not been so dedicated, and is instead sought for permanent proprietary use. Thus, it is incorrect to equate, as did the Court of Appeals, common and transient surface street uses with the greatly different character of the subsurface use here.

The Court of Appeals held, as a matter of law,[15] that the lands beneath city streets were "recognized transportation corridors for commerce." App. A-10. But Shell's use of the subsurface differs in material respects from the surface uses that characterize typical transportation cases. It is permanent, rather than transient; it is exclusive, rather than common; and it is private, rather than public. In short, Shell has enjoyed, for the past 47 years, an exclusive proprietary use of city land. And by denying the City's right of reverter, it seeks to transmute its leasehold into a fee.

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[14]However, state autonomy over local transportation facilities will be respected, despite adverse affects on commerce, where regulations advance legitimate local interests, such as safety. *Kassell v. Consolidated Freightways Corp.*, 450 U.S. 662, 670 (1981); *Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 449 (1978) (Blackmun, J. concurring); *Bibb v. Navajo Freight Lines*, 359 U.S. 520, 523-24 (1959) (with respect to highways, a "state has exceptional scope for the exercise of its regulatory power").

[15]There were no findings below to support the court's conclusion.

The nature of Shell's use, perhaps more importantly than its location below the surface, sets it apart from *Cooley*, *Kassell*, and similar transportation cases. Whether Shell lays its pipeline down the center of Main Street, or five feet beneath it, the line is permanently and exclusively occupying land, not sharing a "transportation corridor."[16]

It makes no difference whether Shell is selling artifacts (*San Francisco Street Artists Guild v. Scott*, 37 Cal. App. 3d 667, 670, 112 Cal. Rptr. 502, 504 (1974)), operating a street railway (*Detroit United Ry v. City of Detroit*, 229 U.S. 39 (1913)), or a telegraph system (*St. Louis v. Western Union Tel. Co.*, 149 U.S. 465 (1893)), it has no right to appropriate city streets without permission.

> "[A]ppropriation of [city streets] to private individual uses, from which the public derive no benefit or accommodation, is a perversion of them from their lawful purposes, contrary to the trust imposed in the city authorities. Thus, it is frequently stated that there is no natural right to use the streets for purposes of private business or gain. And it follows as a corollary that the city may forbid any such use. This is a cardinal doctrine of municipal law." 10 McQuillan, *The Law of Municipal*

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[16] Moreover, Santa Monica is not providing a transportation facility; it is providing bare land. It is Shell that owns and operates the transportation facility, albeit not one that is open to the public. Perhaps this explains why common carrier crude oil pipelines, but not proprietary lines, have rights of eminent domain and are regulated in the public interest.

Corporations, §30.73, p. 763 (3d ed. 1981).[17]

It is another matter altogether when Congress grants federal franchises which require use of city streets. *St. Louis v. Western Union Telegraph Co.*, 148 U.S. 92 (1892). But federal franchisees still have to pay for the space in the streets thus exclusively appropriated. *Id.* at 98-101. Even Congressional preemption of franchise terms "does not require a city to renew or to refuse to renew any particular franchise." *Golden State Transit Corp. v. City of Los Angeles*, 475 U.S. 608, 619 (1986). *Accord Williams Pipe Line Co. v. City of Mounds View*, 651 F.Supp. 551, 569 (D.Minn. 1987) (despite extensive federal regulation, "[c]ounty was at no time required to give a hazardous liquid pipeline company the right to lay its line on county property").[18]

By controlling regular street uses, a state has considerable power over the channels of commerce; a power which can be misused for protectionist purposes. The Commerce Clause interposes the federal judiciary between such parochial interests and the nation's interest

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[17]California follows this "cardinal doctrine." *Sunset Telephone & Telegraph Co. v. City of Pasadena*, 161 Cal. 265, 271, 119 P. 796, 798 (1911) (no right to permanently occupy portions of public highways).

[18]If Congress were to require Santa Monica to grant a proprietary franchise to Shell, it might not raise federalism concerns, but it would require just compensation under the Fifth Amendment. *See Block v. North Dakota*, 461 U.S. 273, 291 (1983). The permanent nature of Shell's physical occupation constitutes a *per se* possessory taking. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982). *Accord, St Louis v. Western Union Telegraph Co.*, 148 U.S. at 100-101.

in free trade.[19] But, while streets are unique and indispensable with respect to transient surface uses, they are fungible with other property in their subsurface uses, as is shown by Shell's easements with many public and private landowners.[20] Unlike the "transportation corridor" setting described by the Court of Appeals, this case does not involve discriminatory or burdensome regulations directed at commerce; indeed, it involves no regulations at all.[21]

Shell claims that denial of a lease would force it to find alternative routes at a higher cost. Cert. Pet. at 4. In essence, it views the Commerce Clause as guaranteeing the lowest cost for doing business. Whether

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[19]The primary purpose of the dormant Commerce Clause has been and should be to prevent states from engaging in purposeful economic protectionism. Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 Mich.L.Rev. 1091 (1986).

[20]Shell concedes that it frequently obtains subsurface easements from private parties and does so for other portions of the Ventura line. CR 78:156, 167-69.

[21]This case is thus distinguishable from *West v. Kansas Natural Gas Co.*, 221 U.S. 229 (1911), cited by the court as authority for requiring Santa Monica to issue a franchise. There, this Court invalidated a state law prohibiting natural gas pipeline easements across state highways. However, the key ingredient was not the use of highways, but the state's designation of those of its highways which formed state lines as absolute barriers to commerce. As was explained in a later appeal of *West*, the law was integral to a state scheme to prevent the exportation of natural gas. *Haskell v. Kansas Natural Gas Co.*, 224 U.S. 217, 221 (1912). *See also Kansas City Gas Co. v. Kansas City*, 198 F. 500, 518 (W.D. Mo. 1912) ("the purpose of the law after all, masked as it was, contemplated solely and chiefly the prevention of the exportation of gas from the state").

Notably, in these cases, the Court did not consider the "extent of the rights of public or private ownership [of highways] in the State of Oklahoma." *Haskell* at 221.

the claim is protective of shareholders, employees, or consumers, it is misplaced. *Commonwealth Edison v. Montana*, 453 U.S. at 619 ("Commerce Clause [does not give] residents of one State a right of access at 'reasonable' prices to resources located in another State").

This case thus reduces to whether the dormant Commerce Clause requires a state to "surrender" property rights for the private economic benefit of a company engaged in commerce. The "novelty" of the case is Shell's characterization of a possible denial of lease rights "as a burden which the Commerce Clause was intended to make suspect." *Hughes v. Alexandria Scrap*, 426 U.S. 794, 807 (1976). As with fundamental rights analysis under the due process clause,[22] Shell may not claim a constitutional entitlement to governmental benefits which might assist it in carrying on its commercial activities. Just as the "Due Process clause . . . does not confer an entitlement to such funds as may be necessary to realize all the advantages of that freedom," *Harris v. McRae*, 448 U.S. 297, 317-18 (1980), neither does the Commerce Clause confer an entitlement to government property.

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[22]In other contexts, this Court has recognized a sharp distinction between state action burdening the exercise of protected rights and a state's refusal to facilitate their exercise. *See, e.g., Maher v. Roe*, 432 U.S. 464 (1977).

CONCLUSION

For the foregoing reasons, it is respectfully requested that, in the event the Petition for Writ of Certiorari is granted, the Court grant this Cross-Petition as well.

Dated: May 9, 1988

Respectfully submitted,

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PROOF OF SERVICE BY MAIL

State of California

ss.

County of Los Angeles

I, the undersigned, say: I am and was at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, over the age of eighteen (18) years and not a party to the within action or proceeding; that my business address is 11333 Iowa Avenue, Los Angeles, California 90025; that on May 9, 1988, I served the within *Cross Petition for Writ of Certiorari* in said action or proceeding by depositing true copies thereof, enclosed in a sealed envelope with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

Clerk, United States
Supreme Court
One First Street, N.W.
Washington, D.C. 20543
(Original and forty copies)

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All parties required to be served have been served. I declare under penalty of perjury that the foregoing is true and correct. Executed on May 9, 1988, at Los Angeles, California.

Siri Ved K. Khalsa
(Original signed)

Supreme Court, U.S.
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IN THE

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OCTOBER TERM, 1987

CITY OF SANTA MONICA,
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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION TO CROSS-PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Shell disagrees with cross-petitioner's statement of the questions presented. Shell believes the cross-petition presents only one issue:

> Whether conditions imposed by a city upon an interstate pipeline's use of the subsurface of public streets are subject to Commerce Clause scrutiny.

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No. 87-1841

IN THE

Supreme Court of the United States

October Term, 1987

CITY OF SANTA MONICA,
Petitioner,
vs.

SHELL OIL COMPANY,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION TO CROSS-PETITION FOR WRIT OF CERTIORARI

PRELIMINARY STATEMENT

In its Cross-Petition, Santa Monica argues that the market participant exception to the dormant Commerce Clause applies in the case at bench. This argument is also championed — and the real reasons therefore made clear — by the City's three *amici*. Confronted with the effect of a California initiative measure that amended the California Constitution and limited local governments' power to levy taxes on their own citizens, the cities hope to collect additional fees from interstate commerce. They realize that the resulting Commerce Clause problems can be avoided if

Cities are held to be mere "market participants" and thus exempt from Commerce Clause scrutiny as they impose user fees for the use of the subsurface of city streets.

As some members of this Court and the City's *amici* have recognized, "the precise contours of the market participant doctrine have yet to be established . . . ." *South-Central Timber Development, Inc. v. Wunnicke*, 467 U.S. 82, 93, 81 L.Ed.2d 71, 104 S.Ct. 2237 (1984). (Plurality opinion.) Absent an opinion from this Court holding that they are constrained by the Commerce Clause when they impose user fees for the use of the subsurface of public streets, local governments will be encouraged to solve their local revenue problems by imposing excessive fees on interstate commerce.

Petitioner and cross-respondent Shell Oil Company ("Shell")[1] strongly urges the Court to grant the cross-petition in this case but for reasons different from those asserted by cross-petitioners. This petition should be granted but only in connection with a grant of the Petition for Writ of Certiorari in Case No. 87-1685 so that this Court can fully address the problem.

CONSTITUTIONAL PROVISIONS INVOLVED

Two provisions of the United States Constitution are relevant to this case:

1. The Commerce Clause, article I, section 8, clause 3:

> "The Congress shall have Power . . . to regulate Commerce . . . among the several States, ..."

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[1] Shell hereby incorporates by reference the List Pursuant to Supreme Court Rule 28.1, set forth at pages iii-x of its Petition for Writ of Certiorari in Case No. 87-1685.

2. The Supremacy Clause, article VI, clause 2:

> "This Constitution . . . shall be the supreme Law of the Land; . . . ."

Shell does not agree that this case raises issues under the Tenth Amendment to the United States Constitution.

STATEMENT OF THE CASE

Shell incorporates by reference the statement of the case contained in its Petition for Writ of Certiorari in Case No. 87-1685. In addition, Shell responds to two erroneous statements made by the City in its statement of the case:

First, Shell does *not* claim a right to lease the subsurface of city streets for a nominal fee. Shell claims a right, as recognized by this Court, to pay a reasonable fee to the City for the use of the subsurface of the streets.[2]

Second, Shell has never claimed any right tantamount to eminent domain, or claimed the power to appropriate a permanent exclusive right in the subsurface. Rather, Shell has maintained that its use is always subject to reasonable non-preempted regulation by the City. Shell has also recognized the possibility that in the future Santa Monica might be justified in refusing to renew the franchise if, for example, numerous other oil pipeline operators apply for franchises in the same location, or if the pipeline interferes with other proper street purposes (which it does not). *See*, Shell's Reply Brief in the Ninth Circuit, at 17.

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[2] *See*, Petition for Writ of Certiorari in Case No. 87-1685, section I.

REASONS FOR GRANTING OR DENYING THE PETITION

I.

THE CITY OF SANTA MONICA AND ITS AMICI SEEK TO AMELIORATE THEIR FINANCIAL PROBLEMS BY IMPOSING FEES ON INTERSTATE COMMERCE

The City's *amici* demonstrate the purpose behind the cities' desire to be free of Commerce Clause restraints when imposing user fees for the use of the subsurface of city streets. They point to a California tax reform initiative which has "greatly restricted the power of California cities to raise revenues by taxation." California Constitution, article XIII A.

The year 1978 saw the culmination of a "taxpayers' revolt" in California. This revolt was caused by a dramatic increase in the property tax burden placed on California homeowners. In the sixteen years prior to 1978, "assessed values in California tripled, tax rates increased by 51 percent, and property taxes themselves more than quadrupled." California voters enacted "Proposition 13," an amendment which added article XIII A to the State Constitution which limited the taxes assessed by local governments. K. Ehrman & S. Flavin, *Taxing California Property* (2d ed. 1979) pp. 28-32. Broadly speaking, article XIII A limits property taxes to one percent of a property's value at the date of acquisition plus an annual inflation factor of no more than two percent. In addition, it prohibits the imposition of new local special taxes except upon an affirmative vote of 2/3's of the electorate and prohibits any new local real property ad valorem taxes or any new sales taxes on the sale of real property.

By their use of the political process, the citizens of the various local cities are thus able to insulate themselves against local taxation. As a result, the cities themselves are encouraged to find means of raising revenues from entities, such as interstate pipeline operators, which are unrepresented in the local citizenry. Here, the Shell Oil Company pipeline is such a target.

Cases such as this, where the burden on interstate commerce is placed on an entity which is unrepresented in the local citizenry and where there is no local proxy that will effectively represent its interests, are particularly appropriate cases for Supreme Court review under the Commerce Clause. Without such review, the purposes of the Commerce Clause will be frustrated and "economic Balkanization" will result. *Southern Pacific Company v. Arizona*, 325 U.S. 761, 767-768 n. 2, 89 L.Ed. 1915, 65 S.Ct. 1515 (1945); L. Tribe, *American Constitutional Law* (2d ed. 1988) § 6-5 ; 1 R. Rotunda, J. Nowak & J. Young, *Treatise on Constitutional Law* (1988 Supp.) § 11.11; Rotunda, *The Doctrine of the Inner Political Check, the Dormant Commerce Clause, and Federal Preemption* (1986), 53 Transport. Pract. J. 263.

II.

THE CITY ACTS AS A MARKET REGULATOR, NOT A MARKET PARTICIPANT, WHEN IT ISSUES FRANCHISES FOR PIPELINE USE OF CITY STREETS

When Santa Monica issues a franchise for pipeline use of the City streets, it is acting as a market regulator, not a market participant.

Cases decided by this Court establish a distinction between state and local governments acting as "regulators,"

and state and local governments acting as "market participants." *White v. Massachusetts Counsel of Construction Employers, Inc.*, 460 U.S. 204, 75 L.Ed.2d 1, 103 S.Ct. 1042 (1983); *Reeves' Inc. v. Stake*, 447 U.S. 429, 65 L.Ed. 2d 244, 100 S.Ct. 2271 (1980); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 49 L.Ed.2d 220, 96 S.Ct. 2488 (1976). *See also, South-Central Timber Development, Inc. v. Wunnicke*, 467 U.S. 82, 81 L.Ed. 2d 71, 104 S.Ct. 2237 (1984). When local governments act as "market participants," they are not subject to Commerce Clause scrutiny. When they act as "regulators," they are.

The distinction between acting as "regulators" and acting as "market participants" is nothing more than a common sense recognition that from time to time state or local governments depart from their traditional roles as governmental bodies and engage as business people in the market place. When they are in their governmental role, we call them "regulators" and they are governed by the rules applicable to governments. On the other hand, when they engage as business people in the market place, we refer to them as "market participants" and they are then governed by the rules applicable to business people and not by the rules applicable to governments. For example, the antitrust laws apply to a state when it is acting as a market participant but not when it is acting in its governmental capacity. In this regard, *see Jefferson County Pharmaceutical Association, Inc. v. Abbott Laboratories*, 460 U.S. 150, 154, 74 L.Ed.2d 882, 103 S.Ct. 1011 (1983)(where it was held that state action immunity under the antitrust laws does not apply where a state has chosen to compete in the private retail market). Also, *see Parker v. Brown*, 317 U.S. 341, 350-352, 87 L.Ed. 315, 63 S.Ct. 307 (1943)(where it was held that when the state acts as a market regulator, it is immune from antitrust scrutiny).

In the case at bench, the City of Santa Monica is acting as a regulator and not as a market participant.

A. The City Only Holds The Property In Question For Street Purposes, Not As Its Own Property To Do With As It Wishes. This Militates Against Application Of The Market Participant Doctrine And In Favor Of Treating The City As A Regulator.

Here, the City of Santa Monica seems to base its argument that it is a market participant on the theory that it "owns" the streets. This is certainly not the case. All cities, Santa Monica included, hold streets in trust for the public, for street purposes. This rule is stated in *Mervynne v. Acker*, 189 Cal.App.2d 558, 561, 11 Cal.Rptr. 340 (1961):

> ". . . Public highways belong to all the people of the state. Every citizen has the right to use them, subject to legislative regulation. . . ."

The same rule is stated by McQuillen:

> ". . . Whatever may be the quality or quantity of the estate of the city in its streets, that estate is essentially public and not private property, and the city in holding it is considered the agent and trustee of the public and not a private owner for profit or emolument. . . ."

10 E. McQuillen, *The Law of Municipal Corporations* (3d ed. 1978), § 30.40 at 685. Not only are streets held in trust for public use, but the public use is that of the entire public, not just the municipality where the streets are located. Thus, McQuillen states at page 686:

> ". . . 'Streets are for the public use, but do not exist for the use of the municipality in which they are situated alone or its inhabitants.'. . . ."

Elsewhere, at pages 762-763 in Section 30.73, McQuillen elaborates further:

> ". . . The streets and public ways of a municipal corporation are held by it in trust for the public, to be used for the ordinary purposes of travel and such other uses as customarily pertain thereto *which, in recent years, are numerous and various.* . . ." (Emphasis supplied.)

There is no doubt that pipelines are proper and accepted street uses in California. The City cannot reasonably dispute that pipelines are commonly found in the subsurface of the City streets. For example, both Shell's pipeline and the local gas utility pipeline utilize the subsurface of the city streets in Santa Monica. Furthermore, California Public Utilities Code section 6202 acknowledges that oil pipeline uses are proper street purposes:

> "The legislative body of any municipality may grant a franchise . . . to use, or to lay and use, pipes and appurtenances for transmitting and distributing oil . . . ."

The City of Santa Monica does not own the streets in fee. It merely owns an easement for street purposes. C.R. 80:52. Thus, whether the City purports to be controlling the surface of the city streets or the subsurface of the city streets, its only title is for "street purposes." Nevertheless, the City clearly purports to not only exercise control over the surface of the streets but also control over the subsurface. It thus exercises the power to franchise the use of the subsurface of city streets for pipeline purposes. Indeed, the City has done so for many, many years as have virtually all other cities and counties in the State of California. It follows that pipeline usage of streets is a valid and accepted street use. Were that not so, cities would be powerless to grant pipeline franchises.

The City is, therefore, not dealing with its own property as a market participant when it grants franchises for pipeline purposes. It is dealing with public property which it holds in trust for all members of the public who, subject to reasonable regulation, are all entitled to reasonable use of the streets for proper street purposes. In short, the City is *regulating* the use of the streets.

B. The Market Participant Doctrine Has No Place Where The Governmental Entity Has Monopoly Power Over A Finite Resource.

Application of the market participant doctrine assumes that the governmental entity involved is simply one of many participants in the market_ place. It has no rational application where the governmental entity has monopoly power over a finite resource. The City of Santa Monica acknowledges this rule at page 6 of its Cross-Petition.

Here, the City of Santa Monica has a practical monopoly over pipeline routes within the City (a finite resource) because there is no viable alternative pipeline right of way for Shell other than the subsurface of the streets. In heavily urbanized areas, one cannot run a pipeline without making use of the city streets. In such areas, ownership of private land is so widely distributed and the parcels are so intensely developed that it is virtually impossible to assemble a pipeline right of way without using the city streets. Furthermore, even if a sufficient number of contiguous private parcels could be assembled, it would still be necessary to cross under public streets at the end of each city block. Public streets, therefore, are quite unique, indispensable and finite when it comes to subsurface pipeline transportation.

Although Santa Monica asserts that it does not have monopoly power over Shell, that is not the case. The City

does have monopoly power over Shell in a number of ways. First, it straddles and divides the 82.2 mile pipeline that stretches from Ventura to Shell's Wilmington refinery, near Long Beach, California. The cost to relocate the pipeline segment that runs through the City to a route outside of Santa Monica, if such relocation were possible, is approximately $2,500,000, exclusive of right of way acquisition costs. C.R. 80:64-66. Thus, when the City "competes" in the right of way market (assuming there really is such a "market"), it enjoys a $2,500,000 bargaining advantage over its "competitors." Such an advantage clearly gives the City market control and, thus, a practical monopoly up to $2,500,000.

This monopoly could not be broken by Shell's attempting to move its oil by tank truck or marine tanker or barge. To begin with, it is not economically feasible to move the oil by truck. At the present through-put rate of the subject pipeline, approximately 170 tanker trucks per day would be needed to transport the oil at a cost increase of approximately $1.36 per barrel. C.R. 80:45-46. Assuming 30,000 barrels of crude oil per day, simple mathematics show that the additional annual cost of such a project would be approximately $14,892,000. Furthermore, shipping the oil from Ventura by barge or marine tanker would simply not be feasible because of the lack of facilities located near the refinery that can handle the size and type of tanker which can be loaded with crude oil at Ventura. C.R. 80:46-47. Shell could not make arrangements to hire an existing public utility pipeline to carry Shell's oil for a fee even though the City of Santa Monica suggests that it could. There is absolutely no evidence in the record of the existence of any such public utility pipeline and — in fact — there are no such lines between Ventura and Wilmington.

In truth, these alternatives are not really alternatives at all. Oil pipelines are the safest mode for transporting

petroleum, one thousand times safer than trucks. *Oil Pipelines of the United States: Progress and Outlook* 15 (Assoc. of Oil Pipelines, 1983). Oil pipeline transportation charges are extremely low. *Id.* at 8, 16. Pipelines are "the most economical means of moving large volumes of petroleum overland for long distances . . . ." *Id.* at 2. Santa Monica's actions in this case and its argument that the market participant exception applies, ignores these facts and refers to "alternatives" without recognizing that those other modes of transportation are *not* reasonable substitutes for pipelines, and that the moving of an oil pipeline, when possible, is extremely expensive.[3]

The City, therefore, does have absolute power over the "price" charged for the franchise, at least up to the point where the franchise fee makes unreasonable and uneconomical alternatives attractive. This is a powerful demonstration of the City's monopoly power over Shell. *See*, R. Posner & F. Easterbrook, *Antitrust Cases, Economic Notes*, and other materials 360-362 (1981); L. Sullivan, *Handbook of the Law of Antitrust* 57 (1977); Landes and

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[3] The Commerce Clause is concerned with increased costs of transportation caused by state or local governments. In *Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 438-439, 445-446, 54 L.Ed.2d 664, 98 S.Ct. 787 (1978), the Court struck down a state statute that forced a truck carrier to use different types of trucks within the state than those normally used by the carrier or to use the desired trucks in a different manner. In part, the *Raymond* court was concerned with the substantial increase in cost to move goods in interstate commerce which resulted from the operation of the statute. Another case is *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 674, 686, 67 L.Ed.2d 580, 101 S.Ct. 1309 (1981)(State law forced change in manner of transporting goods in interstate commerce; law added approximately $12,600,000 to the costs of all trucking companies doing business in state. Approximately $2,000,000 of that increase was borne by Consolidated. The Court also pointed out that interstate commerce could not be forced to bypass the state.).

Posner, *Market Power in Antitrust Cases*, 94 Harv.L.Rev. 937, 960-961 (1981); Turner, *Antitrust Policy* and the cellophane *Case*, 70 Harv.L.Rev. 281 (1956). As Judge Learned Hand recognized: "There are indeed limits to . . . power; substitutes are available for almost all commodities, and to raise the price enough is to evoke them." *United States v. Aluminum Company of America*, 148 F.2d 416, 425-426 (2d Cir. 1945).

The Ninth Circuit clearly recognized that because here traditional transportation corridors were involved and because of the City's practical monopoly power with respect to those transportation corridors, the City was not a market participant but instead was a regulator subject to scrutiny under the Commerce Clause. Ordinarily, that would be a sufficient basis for denying the City's Cross-Petition. The fact, however, that the City of Santa Monica (supported by its three *amici* cities) seeks to apply the market participant doctrine as a means of avoiding Commerce Clause scrutiny in its efforts to collect additional fees from interstate commerce is a sound reason for this Court's granting certiorari in both Case No. 87-1685 and in this case. It is important that this Court make it clear that under *no* theory may cities use their control over the subsurface of city streets to exact tribute from the interstate transport of commodities via subsurface pipelines.

CONCLUSION

For all the above reasons, this Court should grant certiorari in this case, but for reasons different than those asserted by the City of Santa Monica and its *amici*. Instead, the cross-petition should be granted but only in connection with the petition in Case No. 87-1685 so that this Court can fully consider the burden imposed on interstate commerce by the City's actions.

DATED: June 9, 1988

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